FAA's saving clause. *Morales*, 504 U.S. at 378; *see Wolens*, 513 U.S. at 222.

In 1978, Congress enacted the ADA, 92 Stat. 1705, which largely deregulated the interstate airline industry. *Wolens*, 513 U.S. at 222; *Morales*, 504 U.S. at 378. Congress enacted the ADA upon "determining that 'maximum reliance on competitive market forces' would best further 'efficiency, innovation, and low prices' as well as 'variety [and] quality ... of air transportation services[.]' " *Morales*, 504 U.S. at 378 (quoting 49 U.S.C. §§ 1302(a)(4), 1302(a)(9)); *accord Wolens*, 513 U.S. at 230.

To ensure the states would not undo federal deregulation by putting in place regulation of their own, Congress inserted a preemption clause into the ADA. *Wolens*, 513 U.S. at 222; *Morales*, 504 U.S. at 378. In its original version, the clause provided: "No state ... shall enact or enforce any law, rule, regulation, standard, or other provision having the force and effect of law relating to rates, routes, or services of any air carrier ...." 49 U.S.C.App. § 1305(a)(1). The clause's current version differs from the original one in form but not in substance. *See Wolens*, 513 U.S. at 223 n.1. It states: "[A] state ... may not enact or enforce a law, regulation, or other provision having the force and effect of law related to a price, route, or service of an air carrier ...." 49 U.S.C. § 41713(b)(1). Importantly, when it inserted the preemption clause into the ADA, however, Congress did not repeal the FAA's saving clause, but instead retained it. *Wolens*, 513 U.S. at 232; *Morales*, 504 U.S. at 379.

As indicated, the ADA's preemption clause prohibits a state from enacting or enforcing "law" that is "related to" an air carrier's prices, routes, or services. Under that clause, state law is "related to" an air carrier's prices, routes, or services if it has a "connection with, or reference to," *Morales*, 504 U.S. at 384; *accord Wolens*, 513 U.S. at 223,

prices, routes, or services. A state law's "reference" to prices, routes, or services is largely a matter of words, and may be either express or implied. *See Morales*, 504 U.S. at 388. By contrast, a state law "connection with" prices, routes, or services is essentially practical. *See Wolens*, 513 U.S. at 224; *Morales*, 504 U.S. at 388. A state law has the requisite "connection" if it has a "significant effect" "as an economic matter." *Morales*, 504 U.S. at 388. Contrariwise, a state law does not have such a "connection" if it is " 'too tenuous, remote, or peripheral . . . to have [such an] effect.' " *Wolens*, 513 U.S. at 224 (quoting *Morales*, 504 U.S. at 390, but omitting internal quotation marks).

Under the ADA's preemption clause, the "law" that a state is prohibited from enacting or enforcing is one that imposes obligations on parties as a matter of public policy independent of any contract into which the parties have freely entered. *See Wolens*, 513 U.S. at 229 n.5 (a preempted state law must involve "official, government-imposed policies, not the terms of a private contract," and must comprise "binding standards of conduct that operate irrespective of any private agreement" (internal quotation marks omitted)). By contrast, the "law" that a state may enact and enforce without fear of preemption is one that governs contracts into which parties have freely entered—the law of contracts in its general principles. *See id.* at 233 n.8 (implying there is no preemption of a state law that is consistent with general contract law principles and "not at its core diverse, nonuniform, and confusing").

Because the ADA's preemption clause does not prohibit a state from enacting or enforcing its contract law even insofar as it relates to an air carrier's prices, routes, or services, the clause does not prohibit a state from granting relief in a contract action brought under such law. As noted, the ADA was "designed [by Congress] to promote 'maximum reliance on competitive market forces.' . . .

Market efficiency requires effective means to enforce private agreements. . . . 'The stability and efficiency of the market depend fundamentally on the enforcement of agreements freely made, based on needs perceived by the contracting parties at the time.' " *Wolens*, 513 U.S. at 230. Congress did not entrust the enforcement of such contracts to the CAB in earlier times nor has Congress entrusted such enforcement to the DOT today. *See id.* at 232. Neither has Congress "channel[ed] into federal courts the business of resolving, pursuant to judicially fashioned federal common law, the range of contract claims" in this area. *Id.*

The ADA therefore "permits state-law-based court adjudication of routine breach-of-contract claims . . . ." *Wolens*, 513 U.S. at 232. This "conclusion . . . makes sense of Congress' retention of the FAA's saving clause . . . ." *Id.* "The ADA's preemption clause . . . , read together with the FAA's saving clause, stops States from imposing their own substantive standards with respect to rates, routes, or services, but not from affording relief to a party who claims and proves that an airline dishonored a term the airline itself stipulated." *Id.* at 232-33. "This distinction between what the State dictates and what the airline itself undertakes confines courts, in breach-of-contract actions, to the parties' bargain [under state contract law], with no enlargement or enhancement based on state laws or policies external to the agreement." *Id.* at 233.

In accordance with the above analysis, this Court resolved the issues presented in *Morales* and *Wolens* as follows.

Morales involved so-called Air Travel Industry Enforcement Guidelines (Guidelines), adopted by the National Association of Attorneys General (NAAG), which contained detailed standards governing the content and format of airline fare advertising. *Morales*, 504 U.S. at 383-

91. *Morales* held the ADA's preemption clause prohibited enforcement of the Guidelines through a state's general consumer protection law. It reasoned that insofar as the Guidelines operated as law in a state enforcement action, they related to an air carrier's "prices" because they had a "reference to airfares"—indeed, an "express reference." It also reasoned that the Guidelines had a connection with airfares inasmuch as they had the "forbidden significant effect upon fares" by imposing "restrictions on fare advertising" and thereby "serv[ing] to increase the difficulty of discovering the lowest cost seller . . . and [to reduce] the incentive to price competitively." *Id.* at 388 (internal quotation marks omitted).

Wolens involved state-court class actions brought on behalf of participants in an airline's frequent flyer program, challenging retroactive changes by the airline in program terms and conditions as a violation of the state's consumer fraud statute and also as a breach of contract under state contract law. 513 U.S. at 224-25. At the outset, *Wolen* held that both the consumer-fraud and the breach-of-contract claims "relate to 'rates,' *i.e.*, . . . charges in the form of mileage credits for free tickets and upgrades, and to 'services,' *i.e.*, access to flights and class-of-service upgrades . . . ." *Id.* at 226. *Wolens* then articulated a two-pronged holding. First, it held the ADA's preemption clause prohibited enforcement of the state consumer fraud statute because it came with the clause's scope as relating to "rates" and "services." *Id.* at 227-28. However, it then held that clause did not prohibit enforcement of state contract law, even though that law similarly related to "rates" and "services." *Id.* at 228-35. In carving out an exception for state contract law, it reasoned that although the clause barred enforcement of the state consumer fraud statute, because that statute did "not simply give effect to bargains offered by the airlines and accepted by airline customers" [*id.* at 228], the

clause allowed enforcement of state contract law, whose sole purpose was to give effect to such bargains. *Id.* at 228, 229. After all, *Wolens* said, state contract law "simply holds parties to their agreements—in this instance, to business judgments an airline made public about its rates and services." *Id.* at 229.

In the present case, FedEx, an air carrier, voluntarily entered into a contract with PSL, a supplier of electronic equipment, agreeing, for a fee, to transport a prototype piece of electronic equipment from PSL's factory in Emeryville, California, to San Diego, California. This was the contract of carriage. (App. 2) Federal Express's airbill, which reflected the contract of carriage, provided in pertinent part:

> Our liability in connection with this shipment is limited to the lesser of your actual damages or $100, unless you declare a higher value, pay an additional charge, and document your actual loss in a timely manner. You may pay an additional charge for each additional $100 of declared value. The declared value does not constitute, nor do we provide, cargo liability insurance. [¶] In any event, we will not be liable for any damage, whether direct, incidental, special, or consequential in excess of the declared value of a shipment, whether or not Federal Express had knowledge that such damages might be incurred including but not limited to loss of income or profits. . . . For us to process your claim, you must make the original shipping cartons and packing available for inspection.

(App. 2)

Alongside the contract of carriage, FedEx freely entered into a separate contract with PSL. Under this latter contract, FedEx agreed, for a separate fee, to provide $20,000 of additional "declared value" coverage for damage to PSL's

electronic equipment and to adjust any claim relating to such damage. (App. 2-3) It is undisputed that implicit in the contract was a promise to adjust any such claim in a reasonable manner and in a reasonable time. This was the contract of reasonable claims-adjustment.

During transport by FedEx, PSL's equipment suffered extensive damage. (App. 2) After learning about the damage, PSL repeatedly communicated with FedEx about the matter. FedEx repeatedly assured PSL that it did not need to have the equipment inspected but needed only to have it repaired and then submit a claim for reimbursement. (App. 2-3)

PSL had the equipment repaired at a cost of $17,450 and submitted a claim to FedEx for that amount. (App. 3) FedEx then denied the claim because the equipment had not been inspected before repair. (App. 3) For several months, PSL repeatedly asked FedEx to change its position, but FedEx refused. (App. 3) Instead, FedEx informed PSL that "the only way FedEx pays claims like this is if you sue us." (App. 3)

PSL reluctantly then filed an action against FedEx in the California Superior Court for Alameda County, asserting claims for breach of contract and breach of the covenant of good faith and fair dealing. (App. 1, 3) Six weeks before the scheduled commencement of trial, and after extensive litigation, FedEx reimbursed PSL for the cost of repairing its equipment ($17,450) and refunded the $959.45 PSL originally paid to ship the equipment. (App. 3) By that time, however, PSL had incurred more than $78,000 in attorney's fees in its effort to compel FedEx to pay the claim that FedEx initially refused to pay and only dilatorily paid. (App. 3)

Proceeding to trial, PSL proved to a jury that FedEx had breached its contract of reasonable claims-adjustment. The

jury awarded PSL $78,027.08 in compensatory damages, consisting of "the amount of attorney's fees ... [PSL] reasonably incurred to collect the benefits due under the contract." (App. 3) PSL also proved to the jury that FedEx had breached the covenant of good faith and fair dealing. (App. 3) Finding that FedEx had acted with fraud, oppression, or malice in breaching that covenant, the jury awarded PSL $1.5 million in punitive damages. (App. 3) PSL consented to a $900,000 reduction of the punitive damages to $600,000 to avoid a new trial that the trial court had conditionally granted. (App. 3) The trial court rendered judgment accordingly. (App. 1, 3)

On FedEx's appeal, in a published opinion, the California Court of Appeal, First Appellate District, Division Four, reversed the judgment. The Court agreed with FedEx that the ADA's preemption clause and the federal common law declared or released value doctrine barred the action in toto. (App. 3-4)

As to the ADA's preemption clause, the Court of Appeal reasoned that the term "services" in that clause extended to the adjustment of claims under FedEx's separate contract of reasonable claims-adjustment. (App. 7-8) On that basis, it held that PSL's claim for breach of that contract was impermissible as not "routine." (App. 8) It also held that PSL's claim for breach of the covenant of good faith and fair dealing, including the availability of punitive damages, was impermissible as well. (App. 10-11) In addition, it found the declared or released value doctrine barred any damages award because FedEx had made full payment to PSL for the damage to its equipment. (App. 15-18) As to both issues, the Court noted, however, that "[a]lthough the supremacy of federal law requires that Federal Express prevail, we cannot refrain from expressing our dismay at this result." (App. 18)

PSL filed a petition for rehearing in the California Court of Appeal, which that Court summarily denied. (App. 20) PSL then filed a petition for review in the California Supreme Court, which that Court denied. (App. 21)

As shown below, because the California Court of Appeal's decision is erroneous on two important issues involving the meaning of the ADA's preemption clause, and because the declared or released value doctrine was not a bar to recovery, this Court should grant the petition.

VI.

REASONS FOR GRANTING THE PETITION

In *Morales* and *Wolens*, this Court addressed the purpose and scope of the ADA and its preemption clause, which, as noted, provides that a "state . . . may not . . . enforce a law . . . related to a price, route, or service of an air carrier . . . ." 49 U.S.C. § 41713(b)(1). *Morales* and *Wolens* held that when Congress determined "'maximum reliance on competitive market forces' would best further 'efficiency, innovation, and low prices' as well as 'variety [and] quality . . . of air transportation services' " [*Morales*, 504 U.S. at 378 (quoting 49 U.S.C. §§ 1302(a)(4), 1302(a)(9)); *accord Wolens*, 513 U.S. at 230], Congress intended that the ADA would generally effect federal *de*regulation of the interstate airline industry and that the ADA's preemption clause would specifically prevent state *re*regulation of that industry. In line with Congress' determination favoring the operation of market forces, *Wolens* went on to hold that to permit the operation of such forces, a state (1) may not enforce any law imposed on an air carrier if that law relates to the carrier's prices, routes, or services, but (2) may enforce any law (including its contract law) to which an air carrier freely subjects itself by voluntarily entering into a contract, whether

or not that law relates to the carrier's prices, routes, or services. *Wolens*, 513 U.S. at 232-33.

The present case embraces two important issues involving the ADA's preemption clause.

A. The Meaning Of "Service"

The first issue is the meaning of "service" in the ADA's preemption clause.

Five years ago, in *Northwest Airlines, Inc. v. Duncan*, 531 U.S. 1058 (2000), this Court denied a petition for writ of certiorari presenting the same issue. Joined by Chief Justice Rehnquist and Justice Thomas, Justice O'Connor dissented from the denial of the petition. Justice O'Connor stated her reasons for voting to grant certiorari as follows:

> [The meaning of "service" in the ADA's preemption clause is] important issue that has divided the Courts of Appeals . . . .
>
> We have addressed the scope of the ADA's pre-emption provision on two prior occasions. In *Morales v. Trans World Airlines, Inc.*, 504 U.S. 374, 383 (1992), we noted the "broad pre-emptive purpose" of the ADA. And while we have never directly addressed the definition of "service" . . . , we have suggested that this term encompasses "access to flights and class-of-service upgrades." *American Airlines, Inc. v. Wolens*, 513 U.S. 219, 226 (1995). The Courts of Appeals, however, have taken directly conflicting positions on this question of statutory interpretation.
>
> The Ninth Circuit below, adhering to its decision in *Charas v. TWA*, 160 F. 3d 1259 (1998) (en banc), held that the term "service" encompasses " 'the prices, schedules, origins and destinations of the

point-to-point transportation of passengers, cargo, or mail,' " but not the " 'provision of in-flight beverages, personal assistance to passengers, the handling of luggage, and similar amenities.' " *Duncan v. Northwest Airlines, Inc.*, 208 F. 3d 1112, 1114-1115 (2000) (quoting *Charas, supra,* at 1261). The Third Circuit has expressly agreed with this approach. *Taj Mahal Travel, Inc. v. Delta Airlines Inc.*, 164 F. 3d 186, 194 (1998). In contrast, three Courts of Appeals have adopted a much broader definition. *See Hodges v. Delta Airlines, Inc.*, 44 F. 3d 334, 336 (5th Cir. 1995) (en banc) (defining "service" in terms of the " '[contractual] features of air transportation,' " including " 'ticketing, boarding procedures, provision of food and drink, and baggage handling' "); *Smith v. Comair, Inc.*, 134 F. 3d 254, 259 (4th Cir. 1998) ("Undoubtedly, boarding procedures are a service rendered by an airline") (citing *Hodges, supra,* at 336); *Travel All Over The World, Inc. v. Kingdom of Saudi Arabia*, 73 F. 3d 1423, 1433 (7th Cir. 1996) (adopting *Hodges* definition). *See also Chukwu v. Board of Directors British Airways*, 889 F. Supp. 12, 13 (D. Mass. 1995), *aff'd mem.*, 101 F. 3d 106 (1st Cir. 1996) (same).

Given these opposing interpretations, I believe we should hear this case. The legal issue is an important one, well suited for resolution by this Court. The two leading cases, *Charas* and *Hodges*, are both the product of en banc consideration. They have fully explored the relevant considerations, including the language and history of the ADA and its pre-emption clause, as well as the policies supporting the possible interpretations of the term "service." *Compare*

Charas, supra, at 1262-1266, *with Hodges, supra,* at 336-339.

> Resolution of this question would provide needed certainty to airline companies. . . . Because airline companies operate across state lines, the divergent pre-emption rules formulated by the Courts of Appeals currently operate to expose the airlines to inconsistent state regulations. *Cf. Morales, supra,* at 378 (the ADA's pre-emption provision is intended "[t]o ensure that the States would not undo federal deregulation with regulation of their own").
>
> A decision from this Court would provide needed clarification on this discrete and important issue of statutory interpretation.

Duncan, 531 U.S. at 1058 (mem. of O'Connor, J., dissenting from den. of cert.).

In *Duncan*, Justice O'Connor acknowledged that the issue of the meaning of "service" arose in a narrow factual context—the "potential preemption of a state law personal-injury claim based on an airline's smoking policy." *Duncan*, 531 U.S. at 1058 (mem. of O'Connor, J., dissenting from den. of cert.). Even so, she noted, the case was as appropriate vehicle for deciding that issue since the question involved a purely "legal principle." *Id.*

In the years following *Duncan*, the meaning of "service" has continued to be an important issue, addressed in numerous decisions. These include *Branche v. Airtran Airways, Inc.*, 342 F. 3d 1248 (11th Cir. 2003); *Botz v. Omni Air International*, 286 F. 3d 488 (8th Cir. 2002); *Arapahoe County Public Airport Authority v. Federal Aviation Administration*, 242 F. 3d 1213 (10th Cir. 2001); *New Hampshire Motor Transport Assn. v. Rowe*, 377 F. Supp. 2d 197 (D. Maine 2005); *Williams v. Midwest Airlines, Inc.*, 321

F. Supp. 2d 993 (E.D. Wis. 2004); *Alshrafi v. American Airlines, Inc.*, 321 F. Supp. 2d 150 (D. Mass. 2004); *Garza v. Northwest Airlines, Inc.*, 305 F. Supp. 2d 777 (E.D. Mich. 2004); *All World Professional Travel Services, Inc. v. American Airlines, Inc.*, 282 F. Supp. 2d 1161 (C.D. Cal. 2003); *Skydive Factory, Inc. v. Maine Aviation Corp.*, 268 F. Supp. 2d 61 (D. Maine 2003); *Stone v. Frontier Airlines, Inc.*, 256 F. Supp. 2d 28 (D. Mass. 2002); *De Terra v. America West Airlines, Inc.*, 226 F. Supp. 2d 274 (D. Mass. 2002); *Aquino v. Asiana Airlines, Inc.*, 105 Cal. App. 4th 1272 (2003); *Rubin v. United Airlines, Inc.*, 96 Cal. App. 4th 364 (2002); *Vinnick v. Delta Airlines, Inc.*, 93 Cal. App. 4th 859 (2001); *Townsend v. Delta Airlines, Inc.*, 269 Ga. App. 645 (2004), *cert. granted* (Ga. 2005), & *vacated*, ___ Ga. App. ___, 620 S.E.2d 502 (2005); *Delta Airlines v. Cook*, 816 N.E.2d 448 (Ind. Ct. App. 2004), *adhered to*, 821 N.E.2d 400 (Ind. Ct. App.), *vacated sub nomine Atlantic Coast Airlines v. Cook*, 831 N.E.2d 748 (Ind. 2005); and *Delta Air Lines, Inc. v. Black*, 116 S.W.3d 745 (Tex. 2003). *See generally* Comment, *Federal Preemption of State Law Relating to an Air Carrier's Services*, 71 U. Chi. L. Rev. 1197, 1202-08 (2004) (*Federal Preemption*).

Although—or, perhaps because—the meaning of "service" continues to be an important issue, the federal circuits have not resolved their divisions. Instead, they have been led into further divisions. *See Federal Preemption*, *supra*, 71 U. Chi. L. Rev. at 1198 ("Since [*Duncan*], the disagreement has only broadened."). In *Botz*, 286 F. 3d 488, the Eighth Circuit acknowledged *Charas* and *Hodges*, but ended up following neither, stating merely that "Congress did not choose to restrict the scope" of " 'service[.]' " 286 F. 3d at 494. In *Arapahoe*, 242 F. 3d 1213, the Tenth Circuit cited *Hodges* with approval, but pulled back from embracing it fully, concluding only that " 'service' . . . is . . . intended to include transportation . . . ." 242 F. 3d at 1222. By contrast,

in *Branche*, 342 F. 3d 1248, the Eleventh Circuit appeared at first to have taken sides, stating that it found *Hodges* "more compelling" than *Charas*. 342 F. 3d at 1257. But straightaway, it muddied the waters, defining "service" to include matters "over which air carriers compete" and apparently to exclude matters over which they do not. *Id.* at 1259. *See generally Federal Preemption*, *supra*, 71 U. Chi. L. Rev. at 1202-17.

If clarification about the meaning of "service" was needed in 2000 [*see Duncan*, 531 U.S. at 1058 (mem. of O'Connor, J., dissenting from den. of cert.)], the need is even more acute today. The percolation of the question through lower courts has failed to filter the impurities out of the law and has only increased their presence. Only this Court can provide clarification, and this case is a proper vehicle. Not only is the underlying principle purely legal, but the factual context offers a question worthy of this Court's intervention. Under any reasonable view, an air carrier's performance of a separate contract in which it has voluntarily agreed to reasonably and timely adjust claims for damage to goods is not "service of an air carrier" within the meaning of the ADA's preemption clause.

B. The Effect Of ADA Preemption On State Contract Law

The second issue is the effect of the ADA's preemption clause on state contract law.

As *Morales* and *Wolens* show, in enacting the ADA, Congress chose to regulate the interstate airline industry largely through market forces rather than at the hands of governmental actors. Market forces contemplate that air carriers may freely enter into contracts. And market efficiency, as this Court taught in *Wolens*, requires effective means to enforce such contracts—which Congress has left to

adjudication, principally in state court, based on state contract law. *Wolens*, 513 U.S. at 230, 232. It therefore follows that that the ADA's preemption clause does not displace state contract law.

Although this proposition seems plain, it needs to be made plainer still. *Wolens* states that the preemption clause requires that "breach-of-contract actions" involving air carriers be "confine[d] . . . to the parties' bargain, with no enlargement or enhancement based on state laws . . . external to the agreement." *Wolens*, 513 U.S. at 233. State contract law, of course, is not external to the parties' contract, but gives the contract meaning and effect. The Court of Appeal evidently believed otherwise, stating that this action—which included a claim that FedEx breached its voluntarily-undertaken contract of reasonable claims-adjustment—"should never have been tried." (App. 4)

As *Wolens* explained, the operation of state contract law is necessary to the market-force regulatory regime Congress established in enacting the ADA. Unless that law is allowed to operate, Congress' regulatory regime will be deprived of force. Contract law's free operation, however, is subject to lower court misapprehension, as the Court of Appeal here showed in a published decision. This signals the need for correction. This Court should therefore intervene to reaffirm that the ADA's preemption clause does not displace state contract law.

C. Review Is Warranted Of The Court Of Appeal's Erroneous Holding That "Service" In The ADA's Preemption Clause Includes An Air Carrier's Adjustment Of Contract-Based Property Damage Claims And That The Clause Prohibits State-Based Breach Of Contract And Related Claims

1. The Court Of Appeal Erroneously Defined "Service" In The ADA's Preemption Clause Too Broadly And Therefore Erroneously Barred PSL's Lawsuit

The Court of Appeal held the ADA's preemption clause prohibited PSL's lawsuit in its entirety. This was error warranting review.

Crucial to the Court of Appeal's holding was its interpretation of the term "service" in the ADA's preemption clause. The Court of Appeal acknowledged that the term has been the subject of conflicting definitions. (App. 7) Indeed, as noted, courts across the country are in disarray on that subject. Nevertheless, without analysis, the Court of Appeal applied what it called a "broad" definition, effectively defining the term to extend to anything that an air carrier does with respect to "transportation," including adjusting property damage claims submitted to it under a contract separate from the contract of carriage. (App. 7) Having articulated that broad definition, the Court of Appeal then asserted it was "plain that PSL's lawsuit is about the service Federal Express provides to customers," and "is therefore 'related to a . . . service of an air carrier.' " (App. 7 (quoting 49 U.S.C. § 41713(b)(1)))

This was too broad a reading of "service." If left standing, the definition threatens to prohibit the application of state contract law to all contracts into which an air carrier freely enters—including the reasonable claims-adjustment contract FedEx entered into here. This conflicts with the

holding in *Wolens*, which permits state contract law to operate. As *Charas* explained:

> "[S]ervice[ ]" . . . refers to such things as the frequency and scheduling of transportation, and to the selection of markets to or from which transportation is provided . . . . To interpret "service" more broadly is to ignore the context of its use; and, it effectively would result in the preemption of virtually everything an [air carrier] does. It seems clear . . . that that is not what Congress intended.

160 F. 3d at 1265-66. To interpret "service" to extend to the adjustment of property damage claims would stretch that term to encompass every task an air carrier might happen to perform, from soup to nuts. This is an unreasonable outcome.

Moreover, PSL's lawsuit could not properly be held to be "related to" a "service" that FedEx provides its customers, including the adjustment of claims, unless California contract law has a "connection" with, or "reference" to, such a "service" within the meaning of *Wolens* and *Morales*. Although California law covers all contracts (including presumably claims-adjustment contracts), that law does not "refer" to FedEx's adjustment of claims expressly or by implication. Neither is that law "connected" with FedEx's adjustment of claims. Whether that law could have any "significant effect" on FedEx's adjustment of claims "as an economic matter" [*Morales*, 504 U.S. at 388] is speculative.

The Court of Appeal nevertheless asserted that "it is elemental economics that liability—actual or potential—will impact the rates Federal Express charges for its services." (App. 7) Surely, "all successful . . . suits . . . invariably carry with them an economic cost" for an air carrier. *Duncan v. Northwest Airlines, Inc.*, 208 F. 3d 1112, 1115 (9th Cir.), *cert. den. sub nomine Northwest Airlines, Inc. v.*

Duncan, 531 U.S. 1058 (2000). The same might true even of unsuccessful ones. But the bare existence of actual or potential liability is not enough to trigger preemption. What matters is whether liability will have a *significant* impact—a fact that no record evidence here supports.

Therefore, because the Court of Appeal erred in giving "service" an overbroad reading, it erred in holding PSL's lawsuit barred on that basis.[1]

2. Even If Its Definition of "Service" Was Correct, The Court of Appeal Erred In Barring PSL's California Contract Law Claim For FedEx's Breach Of Its Voluntary Reasonable Claims-Adjustment Contract And The Award Of Compensatory Damages Consisting Of Attorney's Fees

Even if the Court of Appeal was correct in its definition of "service" in the ADA's preemption clause, it was incorrect in the conclusion it reached. As construed in *Wolens* and *Morales*, the clause permits a compensatory

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[1] The Court of Appeal's error extended beyond PSL's claim for breach of contract to the additional claim for breach of the covenant of good faith and fair dealing with its attendant punitive damages award. Contrary to the Court of Appeal's conclusion [App. 10-11], the ADA's preemption clause does not displace California tort law, which in certain circumstances makes punitive damages available for the tortious breach of the covenant of good faith and fair dealing. By its terms, the ADA's preemption clause affects only state law relating to an air carrier's prices, routes, or services. There is no evidence that, to the extent California law permits tort damages for breach of the good faith covenant implied in a reasonable claims-adjustment contract, that law relates to FedEx's prices, routes, or services.

damages award to PSL in the form of attorney's fees for FedEx's breach of its contract of reasonable claims-adjustment. That is because the clause does not prohibit state courts from enforcing their contract law even if that law relates to an air carrier's prices, routes, or services. Thus, the clause does not prohibit a California court from granting relief under California contract law when an air carrier breaches a reasonable claims-adjustment contract.

Consistent with general contract law principles, California law does not impose obligations on parties as a matter of public policy independent of a contract into which the parties freely enter. By definition, a contract entails an "*agreement* to do or not to do a certain thing." Cal. Civ. Code § 1549 (italics added); *see generally* 1 Bernard E. Witkin, Summary of California Law, Contracts, § 1, at 58 (10th ed. 2005); *accord* Restatement (Second) of Contracts § 1 (1981) ("A contract is a promise or a set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty."). It is only after the parties have entered into an agreement that any obligation between them may arise. *See* Cal. Civ. Code §§ 1427, 1428; *see generally* 1 Witkin, *supra*, Contracts, § 1, at 58-59; *accord* Restatement (Second) of Contracts § 1 (duty arises out of, and after, promise). To enter into an agreement, the parties must consent, Cal. Civ. Code § 1550(2), and they must do so freely, *id.* § 1565(1). *See generally* 1 Witkin, *supra*, Contracts, §§ 3, 116, at 61, 155-56; *accord* Restatement (Second) of Contracts § 17 (generally, "formation of a contract requires a bargain in which there is a manifestation of mutual assent").

Neither does California contract law expose parties to damages as a matter of public policy independent of any contract into which the parties have freely entered. Compensatory damages are defined as "compensation . . . in money" that a "person who suffers detriment from the

unlawful act or omission of another" is entitled to "recover from the person in fault." Cal. Civ. Code § 3281; *see generally* 1 Witkin, *supra*, Contracts, § 869 at 956; *accord* Restatement (Second) of Contracts § 346(1) (1981) (generally, an "injured party has a right to damages for any breach by [any other] party"); *id.* § 345(a) ("damages" comprise a "sum of money"). Detriment, in turn, is defined as a "loss or harm suffered in person or property." Cal. Civ. Code § 3282; *accord* Restatement (Second) of Contracts § 346 (1981) ("damages" cover "loss").

Generally, for breach of contract, the "measure of [compensatory] damages . . . is the amount which will compensate the party aggrieved for all the detriment proximately caused thereby . . . ." Cal. Civ. Code § 3300; *see generally* 1 Witkin, *supra*, Contracts, §§ 869-73 at 956-62; *accord* Restatement (Second) of Contracts § 347 (1981) (generally, an "injured party has a right to damages" for "any . . . loss . . . caused by the breach"). In line with their definition, compensatory damages are therefore awarded in breach of contract to compensate a person for the benefit the person would otherwise have received, that is, to give the person the benefit of the bargain. *E.g.*, 1 Witkin, *supra*, Contracts, § 869 at 956; *accord* Restatement (Second) of Contracts § 347 cmt. a (1981) ("Contract damages . . . are intended to give [the injured party] the benefit of his bargain by awarding him a sum of money that will, to the extent possible, put him in as good a position as he would have been in had the contract been performed.").

In this case, FedEx voluntarily entered into a contract of carriage to transport PSL's equipment. FedEx also voluntarily entered into a separate contract of reasonable claims-adjustment to adjust any claim for damage to the equipment in a reasonable fashion and in a reasonable time.

Although FedEx ultimately reimbursed PSL for the damage to its equipment, the ADA's preemption clause did not prohibit the trial court from enforcing California contract law—even insofar as it might have related to FedEx's prices, routes, or services—and from permitting the jury to award damages in the form of the attorney's fees PSL incurred as a proximate result of FedEx's breach of its reasonable claims-adjustment contract. Indeed, the clause invited that result, for it was Congress' design to promote regulation by market forces working principally through state courts under state contract law.

PSL's compensatory damages claim confined itself to the parties' reasonable claims-adjustment contract and FedEx's obligations under California contract law. The claim involved no enlargement or enhancement based on other state law since, as allowed, the claim simply held FedEx to its contract and permitted PSL to recover damages in the form of fees that it was compelled to and did proximately incur to enforce that contract.

In concluding otherwise, the Court of Appeal reasoned that PSL's claim was not "routine" within the meaning of *Wolens*. (App. 7-10) This was error.

Wolens defined a "routine" breach-of-contract claim under state contract law impliedly as one in which a court adjudicates whether an air carrier "dishonored a term the [carrier] itself stipulated." *Wolens*, 513 U.S. at 233.

In imposing liability here, the jury found FedEx failed, indeed refused, to adjust PSL's claim for damage to its equipment in a reasonable and timely fashion. The judgment that followed was without question an "adjudication" that FedEx had "dishonored" its voluntarily-assumed contractual obligation to do so. And the adjudication easily fit *Wolens*'s view of what constitutes a "routine"—and not preempted—breach-of-contract claim.

PSL's claim was also "routine" in outcome, giving rise to compensatory damages to compensate PSL for the detriment proximately caused by FedEx's failure to adjust PSL's claim reasonably. Those damages included the fees PSL was compelled to incur in seeking judicial relief to force FedEx to abide by its contractual obligation. If FedEx had fully performed its contract of reasonable claims-adjustment and had given PSL the benefit of the bargain from the inception, it would have spared PSL the need to incur attorney's fees. But because FedEx breached that contract and deprived PSL of the benefit of its bargain—stating that "the only way FedEx pays claims like this is if you sue us" [App. 3]—it forced PSL to incur attorney's fees to obtain that benefit. PSL was therefore entitled to compensatory damages to cover those fees.

In concluding otherwise, the Court of Appeal looked to *Brandt v. Superior Court*, 37 Cal. 3d 813, 693 P. 2d 796, 210 Cal. Rptr. 211 (1985). *Brandt* held that, under California tort law, an insured may recover as compensatory damages the fees the insured incurs in obtaining benefits due under the insured's policy with the insurer. The Court of Appeal reasoned that PSL's claim for FedEx's breach of its contract of reasonable claims-adjustment was not "routine" on this basis:

> PSL was pursuing recovery of "*Brandt* damages[.]" . . . [¶] *Brandt* damages are not awarded in routine breach-of-contract actions. They are . . . the result of California [tort] law . . . . *Brandt* damages . . . [are] not mentioned in the . . . agreement between PSL and Federal Express. This type of damages is thus not a part of the bargain struck by the parties. It must therefore be regarded as an "enlargement or enhancement based on state law or policies external to the agreement."

(App. 8-10 (quoting *Wolens*, 513 U.S. at 233))

To be sure, PSL's compensatory damages were *similar* to *Brandt* damages in the sense that they covered attorney's fees. The similarity is hardly surprising, since the "measure of [compensatory] damages" for tortious conduct, like the measure of compensatory damages for breach of contract, is generally the "amount which will compensate for all the detriment proximately caused thereby . . . ." Cal. Civ. Code § 3333.

Notwithstanding the similarity, however, PSL's compensatory damages in the form of fees were independently sustainable, based as they were on FedEx's breach of its reasonable claims-adjustment contract. Although not mentioned in that contract, those fees must be considered part of the bargain PSL struck with FedEx. In entering into that contract, FedEx voluntarily obligated itself reasonably to adjust any claim PSL submitted to it. Having refused to do so and having forced—indeed, encouraged—PSL to sue, FedEx triggered a right by PSL to seek assistance from the judicial system and obtain compensatory damages, including the fees it was compelled to incur as a result.

In concluding to the contrary, the Court of Appeal rested on the connection of the parties' contract of reasonable claims-adjustment to their separate contract of carriage. (App. 12-13) True, the former presupposes the existence of the latter. But the two were separate, and FedEx was not required to offer the reasonable claims-adjustment contract to its customers. The ADA's preemption clause did not immunize FedEx from the consequences of its breach of that contract under California contract law. To hold FedEx liable for breaching it did not increase its liability for damage to

PSL's equipment, but simply held it responsible for the damages it proximately caused by its conduct.[2]

3. The Declared Or Released Value Doctrine Cannot Cure The Court of Appeal's Errors

The Court of Appeal concluded that, notwithstanding the ADA's preemption clause, the declared or released value doctrine prohibited the trial court from enforcing California contract law and granting relief for FedEx's breach of its reasonable claims-adjustment contract as well as from

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[2] The Court of Appeal went beyond the ADA's preemption clause to rely—erroneously—on the Carmack Amendment to the Interstate Commerce Act of 1887, Hepburn Act, ch. 3591, 34 Stat. 584, as amended, 49 U.S.C. § 14706. (App. 12-14)

> That Amendment, with preemptive force [*e.g.*, *Adams Express Co. v. Croninger*, 226 U.S. 491, 505 (1913)], limits the liability of a surface carrier for loss or injury to property transported in interstate commerce to the "actual loss or injury to the property" [49 U.S.C. § 14706].

Whether or not the Carmack Amendment applies to an air carrier like FedEx is irrelevant. FedEx's liability for breach of its contract of reasonable claims-adjustment and of the covenant of good faith and fair dealing was not for loss or injury to PSL's equipment, but for the fees it compelled PSL to incur by its refusal to comply with the contractual obligation it voluntarily undertook and for the reprehensibility of its conduct. As such, the Carmack Amendment did not cut off FedEx's liability. *See Gordon v. United Van Lines, Inc.*, 130 F. 3d 282, 284 (7th Cir. 1997) (although "the Carmack Amendment preempts all state law claims based upon the contract of carriage, in which the harm arises out of . . . damage to goods[,] . . . claims involving a separate and independently actionable harm to the shipper distinct from such damage are not preempted").

holding FedEx to the consequences of its breach of the covenant of good faith and faith dealing. (App. 15-18) This conclusion was also erroneous.

The declared or released value doctrine arises from federal common law. *E.g.*, *Kemper Ins. Cos. v. Federal Express Corp.*, 252 F. 3d 509, 512-14 (1st Cir. 2001); *Read-Rite Corp. v. Burlington Air Express, Ltd.*, 186 F. 3d 1190, 1195-98 (9th Cir. 1999); *Sam L. Majors Jewelers v. ABX, Inc.*, 117 F. 3d 922, 926-29 (5th Cir. 1997); *see generally Hart v. Pennsylvania R. Co.*, 112 U.S. 331, 337-38 (1884).

As typically stated, the doctrine "allows" a carrier, including an "air carrier," "to 'limit [its] liability [in a contract of carriage] for injury, loss, or destruction of [property] on a "released valuation" basis.' " *Kemper Ins. Cos.*, 252 F. 3d at 512. "In exchange for a lower shipping rate, the shipper is deemed to have released the carrier from liability beyond a stated amount." *Id.* "However, the shipper is bound by this agreement only if (i) he has reasonable notice of the rate structure and (ii) he is given a fair opportunity to pay a higher rate in order to obtain greater protection." *Id.* If the shipper is provided with such notice and opportunity, his "recovery . . . cannot exceed the released value . . . ." *Deiro v. American Airlines, Inc.*, 816 F. 2d 1360, 1366 (9th Cir. 1987).

The declared or released value doctrine preempts state law within its scope bearing on the liability of an air carrier for any injury, loss, or destruction to property, and thereby prohibits enforcement of state law that would expand the carrier's liability for such injury, loss, or destruction beyond the limit the carrier has properly imposed in a contract of carriage. *E.g.*, *Kemper Ins. Cos.*, 252 F. 3d at 512-14; *Read-Rite Corp.*, 186 F. 3d at 1195-99.

The doctrine did not prohibit PSL from recovering compensatory damages in the form of fees for FedEx's

breach of its reasonable claims-adjustment contract or punitive damages based on the reprehensibility of FedEx's conduct. The doctrine, by its terms, does not preempt state law beyond the limitation in a contract of carriage affecting an air carrier's liability for injury, loss, or destruction to *property*. *See Wayne v. DHL Worldwide Express*, 294 F. 3d 1179, 1185 (9th Cir. 2002) (declared or released value doctrine applies only to "claims for loss of or damage to goods"). FedEx's liability here is for compelling PSL to incur attorney's fees as a proximate cause of FedEx's breach of its reasonable claims-adjustment contract and for the reprehensibility of its conduct; it is not for damage to PSL's equipment. Thus, California law is not preempted.

In concluding to the contrary, the Court of Appeal missed the mark on the law. It cited decisions supporting the proposition that the declared or released value doctrine remains vital following the ADA's enactment. (App. 17 (citing *Read-Rite Corp.*, 186 F. 3d at 1195-97; *Sam L. Majors Jewelers*, 117 F. 3d at 928-929; *First Pennsylvania Bank v. Eastern Airlines, Inc.*, 731 F. 2d 1113, 1122 (3d Cir. 1984); *King Jewelry, Inc. v. Federal Exp. Corp.*, 166 F. Supp. 2d 1280, 1283 (C.D. Cal. 2001); *Welliver v. Federal Exp. Corp.*, 737 F. Supp. 205, 207. (S.D.N.Y. 1990)) The doctrine's vitality, however, is not disputed; what is disputed is its applicability. As explained, by its own terms, the doctrine does not apply where, as here, the air carrier's liability is not for injury, loss, or destruction to *property*. None of the cited decisions holds or states otherwise.

The Court of Appeal also missed the mark on the facts. It cited a decision finding that the declared or released value doctrine effectively limits an air carrier's liability for injury, loss, or destruction to property because the doctrine's conditions had been satisfied. (App. 18 (citing *Read-Rite Corp.*, 186 F. 3d at 1197-98)) That finding is of no consequence here since, as noted, FedEx's liability for

breach of its reasonable claims-adjustment contract and for breach of the covenant of good faith and fair dealing was not for injury, loss, or destruction to property.

VII.

CONCLUSION

This petition presents the Court with an appropriate opportunity to provide necessary clarification of the law respecting the ADA and its preemption clause on the meaning of "service"—a point on which the Courts of Appeals have been in increasing disagreement—and on the scope of that clause as to state breach-of-contract claims—a point that threatens similar disagreement.

This Court should grant this petition, set the case for plenary review, and issue an opinion resolving these questions as urged.

DATED: November 22, 2005

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Filed 3/25/05

CERTIFIED FOR PUBLICATION

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FIRST APPELLATE DISTRICT

DIVISION FOUR

POWER STANDARDS LAB, INC.,
Plaintiff and Respondent,
v.
FEDERAL EXPRESS CORPORATION,
Defendant and Appellant.

A103021

(Alameda County Super. Ct. No. 841-938-1)

Damage to electronic equipment being shipped by defendant Federal Express Corporation (Federal Express) led to litigation that culminated in a judgment in favor of Plaintiff Power Standards Lab, Inc. (PSL) for $78,000 in compensatory damages and $600,000 in punitive damages. The dispositive question is whether federal law—in the form of a preemption provision in the Airline Deregulation Act of 1978 and a doctrine of federal common law—precludes a state court from awarding any relief greater than was expressly and contractually negotiated between the carrier and the shipper. We answer this question in the affirmative. We hold that once the shipper has paid the contractual limit of its liability, state common law and statutory remedies cannot augment that recovery.

BACKGROUND

Because issues of law resolve this appeal, it is not necessary to recount the evidence introduced at the trial

except in the briefest form most favorable to PSL. (*Cassim v. Allstate Ins. Co.* (2004) 33 Cal.4th 780, 787.)

PSL shipped a prototype piece of electronic equipment from its Emeryville factory to San Diego, using Federal Express as the shipper. The shipping air bill stated Federal Express's liability policy:

"Limitations On Our Liability And Liabilities Not Assumed

"Our liability in connection with this shipment is limited to the lesser of your actual damages or $100, unless you declare a higher value, pay an additional charge, and document your actual loss in a timely manner. You may pay an additional charge for each additional $100 of declared value. The declared value does not constitute, nor do we provide, cargo liability insurance. [¶] In any event, we will not be liable for any damage, whether direct, incidental, special, or consequential in excess of the declared value of a shipment, whether or not Federal Express had knowledge that such damages might be incurred including but not limited to loss of income or profits." PSL paid for $20,000 of additional "declared value" coverage from Federal Express.[1] The air bill also set forth the procedures for "Filing A Claim," which included: "For us to process your claim, you must make the original shipping cartons and packing available for inspection."

The shipment arrived badly damaged. PSL's president called Federal Express's 800-telephone number and was repeatedly told that no inspection was necessary,

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1 The invoice value of the equipment was $48,44[illegible].45.

and that after PSL had the equipment repaired, it should submit a claim for the amount of repair expenses. PSL paid $17,450 to have the equipment repaired, and submitted a claim for that amount. Federal Express denied the claim because the equipment had not been inspected before it was repaired. Four months of repeated entreaties produced no change in Federal Express's position. Having been told "the only way FedEx pays claims like this is if you sue us," PSL reluctantly did so.

Six weeks before the scheduled trial date, Federal Express sent PSL a check for $18,409.45 (the $17,450 costs of repair, plus a refund of the $959.45 originally charged to ship the equipment). By that time PSL had incurred more than $78,000 of attorney fees. It therefore proceeded to trial on its causes of action for breach of contract and recovery of attorney fees based upon breach of the covenant of good faith and fair dealing. The jury found that Federal Express breached its contract with PSL, and also breached "the duty of good faith and fair dealing it owed to [PSL] by unreasonably denying the claim." The jury awarded PSL $78,027.08 representing "the amount of attorney's fees . . . [PSL] reasonably incurred to collect the benefits due under the contract." The jury also awarded PSL punitive damages of $1.5 million. The trial court denied Federal Express's motion for judgment notwithstanding the verdict, but it conditionally granted a new trial unless PSL agreed to accept only $600,000 of punitive damages. After PSL consented to this reduction, Federal Express perfected this timely appeal.

REVIEW

Federal Express advances a number of contentions centered on the argument that federal law limited PSL's damages to recovery of no more than PSL's original claim for repair costs of its equipment, which Federal Express paid.

This case should never have been tried because PSL was seeking forms of relief under California law that are precluded by federal law. The Airline Deregulation Act of 1978 (ADA) and two decisions of the United States Supreme Court interpreting the ADA establish that Federal Express cannot be made to pay for more than the declared value of the equipment. The same result is also compelled by the federal common law doctrine limiting a carrier's liability to the value of a shipment declared by a shipper to the carrier. Anything more than the amount of PSL's repair costs, which Federal Express paid prior to trial, cannot be recovered in a California court. As we explain, both of the grounds cited by Federal Express support its argument.

I

The ADA enacted by Congress in 1978 largely deregulated air transport service within the United States. Congress determined that the quality and efficiency of air carrier service would be better promoted by relying on competitive market forces instead of the existing system of pervasive federal regulation. A major congressional concern was that carriers should not be burdened with conflicting state laws and policies that would have adverse economic consequences on the goal of increasing competition among carriers. (See 49 U.S.C. § 40101, subd. (a)(6); H.R. Conf. Rep. No. 95-1779, 95th Cong., 2d Sess., 1, 53 (1978); *American Airlines, Inc. v. Wolens* (1995) 513 U.S. 219, 222, 228, 230; *Morales v. Trans World Airlines, Inc.* (1992) 504 U.S. 374, 378-379.) To avoid state frustration of its purposes, Congress included a provision preempting conflicting state law. In its current version, the provision reads in pertinent part: "[A] State . . . may not enact or enforce a law, regulation, or other provision having the force and effect of law related to a price, route, or service of an air

carrier . . . ." (49 U.S.C. § 41713, subd. (b)(1).) The United States Supreme Court has twice considered the scope of this provision.

In *Morales v. Trans World Airlines, Inc., supra*, 504 U.S. 374, the Attorneys General of seven states notified airlines that they would enforce certain nonstatutory "guidelines" related to the content of the airlines' advertising concerning frequent flyer programs and overbooking. The Court held the guidelines "relat[ed] to" fares and were thus preempted. The Court noted the wide and inclusive scope of the preemption provision; the statute was described as having an " 'expansive sweep' " granted by " 'broadly worded' " language that is " 'deliberately expansive' " and " 'conspicuous for its breadth.' " From this language the Court concluded "State enforcement actions having a connection with, or reference to, airline 'rates, routes or services' are preempted" even if consistent with federal law. (*Id.* at pp. 383-384, 386-387.) The Court further concluded that the states threatened action against what it termed "fare advertising" related to the rates charged by the airlines and was therefore preempted. (*Id.* at pp. 387-391.)

In *American Airlines, Inc. v. Wolens, supra*, 513 U.S. 219, members of an air carrier's frequent flyer program brought suit in state court alleging that a change in the way the program was administered constituted a breach of contract, and violated an Illinois consumer fraud statute. Refusing to retreat from the broadly inclusive reading given the preemption provision in Morales, the Court held that preemption was not restricted to matters that were "essential" to airline operations. "Nonessential" matters were also preempted if they "relate[d] to" the objects of the preemption provision. (*Id.* at p. 226.) The Illinois statute could not be employed because it was intended "to guide and

police the marketing practices of the airlines," a matter "le[ft] largely to the airlines themselves, and not at all to States" by the ADA. (*Id.* at p. 228.)

The breach of contract part of the action, however, was not a "state-imposed obligation" and was thus not preempted. (*American Airlines, Inc. v. Wolens, supra*, 513 U.S. 219, 228-229.) Helpful to understanding what is and what is not prohibited to state involvement is the distinction between what the parties bargain for and what is externally imposed upon that bargain by a state. Terms, conditions, and remedies offered by the carrier and accepted by the customer qualify as "privately ordered obligations," and therefore are not enacted or enforced by the state. (*American Airlines, Inc. v. Wolens, supra*, 513 U.S. 219, 228-229.) "A remedy confined to a contract's terms simply holds parties to their agreements . . . [and] business judgments . . . ." (*Id.* at p. 229.)

These considerations persuaded the United States Supreme Court to formulate the following rule—the preemption provision "permits state-law-based court adjudication of routine breach-of-contract claims" although it "stops States from imposing their own substantive standards with respect to rates, routes, or services, but not from affording relief to a party who claims and proves that an airline dishonored a term the airline itself stipulated. This distinction between what the State dictates and what the airline itself undertakes confines courts, in breach-of-contract actions, to the parties' bargain, with no enlargement or enhancement based on state law or policies external to the agreement." (*American Airlines, Inc. v. Wolens, supra*, 513 U.S. 219, 232-233.) As one federal court held, "when the state begins to change the parties' financial arrangements . . . it is supplying external norms, a process that the national

government has reserved to itself in the air transportation business." (*United Airlines, Inc. v. Mesa Airlines, Inc.* (7th Cir. 2000) 219 F.3d 605, 609-610.)

There is no dispute that Federal Express qualifies as an air carrier for purposes of this provision. (See 49 U.S.C. 40102, subd. (a)(2); *Kemper Ins. Companies v. Federal Exp. Corp.* (1st Cir. 2001) 252 F.3d 509, 512, fn. 3; *Federal Exp. Corp. v. U.S. Postal Service* (W.D. Tenn. 1999) 55 F.Supp.2d 813, 817.) It is equally plain that PSL's lawsuit is about the service Federal Express provides to customers. The essence of that service is the transportation of freight by air. PSL's lawsuit is clearly founded on the unsatisfactory manner in which Federal Express performed that service. It is therefore "related to a . . . service of an air carrier."[2] In addition, it is elemental economics that liability—actual and potential—will impact the rates Federal Express charges for its services.[3] (See *Federal Exp. v. California Public Utilities Com'n* (9th Cir. 1991) 936 F.2d 1075, 1078.) Imposing liability for performance of a carrier's core function would clearly impact the economic ability of that

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[2] Although federal courts have not adopted a uniform definition of what constitutes a carrier's "services" preempted from state interference, a majority of the circuits have given the term a broad construction in keeping with the Supreme Court's decisions in *Morales* and *Wolens*. (See decisions cited in Comment, *Federal Preemption of State Law Relating to an Air Carrier's Services* (2004) 71 U. Chi. L. Rev. 1197, 1202-1208.)

[3] As will be shown in part II, *post*, federal common law has long accepted limiting liability for lost, damaged, or destroyed cargo and personal property as intimately connected to the efficient operation and economic viability of common carriers.

carrier to compete, and thus must be deemed " 'relating to a price . . . or service of an air carrier.' " (E.g., *Read-Rite Corp. v. Burlington Air Express, Ltd.* (9th Cir. 1999) 186 F.3d 1190, 1196-1197; *HIH Marine Ins. Services, Inc. v. Gateway Freight Services* (2002) 96 Cal.App.4th 486, 493-494.)

The contract in this case was the air bill Federal Express issued to PSL. (E.g., *Zubaz, Inc. v. Federal Exp. Corp.* (W.D. Tenn. 1994) 864 F.Supp. 723, 725; *Commodities Recovery Corp. v. Emery Worldwide* (D. N.J. 1991) 756 F.Supp. 210, 212.)[4] At trial PSL was no longer pursuing a routine breach of contract action. Federal Express had already paid the compensatory damages for breach agreed upon by the parties in the contract of carriage. Instead, PSL was pursuing recovery of "*Brandt* fees," named after *Brandt v. Superior Court* (1985) 37 Cal.3d 813. Our Supreme Court recently explained the nature of "*Brandt* damages": "In *Brandt*, this court established a notable exception to [the] rule [i.e., that parties ordinarily pay their own attorney fees] for insurance bad faith cases. We explained that if an insurer fails to act fairly and in good faith when discharging its responsibilities concerning an insurance contract, such breach may result in tort liability for proximately caused damages. Those damages can include

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4 If the airbill incorporates by reference other materials, such as a shipper's service guide, they too are regarded as part of the contract. (E.g., *King Jewelry, Inc. v. Federal Exp. Corp.* (C.D. Cal. 2001) 166 F.Supp.2d 1280, 1284-1285, fn. 3; *Zubaz, Inc. v. Federal Exp. Corp.*, *supra*, 864 F.Supp. 723, 725.) The Federal Express airbill does incorporate its service guide, but the guide did not figure at trial or in the parties' briefs.

the insured's cost to hire an attorney to vindicate the insured's legal rights under the insurance policy. 'When an insurer's tortious conduct reasonably compels the insured to retain an attorney to obtain the benefits due under a policy, it follows that the insurer should be liable in a tort action for that expense. The attorney's fees are an economic loss—damages—proximately caused by the tort. [Citation.] These fees must be distinguished from recovery of attorney's fees qua attorney's fees . . . . What we consider here is attorney's fees that are recoverable as damages resulting from a tort in the same way that medical fees would be part of the damages in a personal injury action.' " (*Cassim v. Allstate Ins. Co., supra*, 33 Cal.4th 780, 806, quoting *Brandt v. Superior Court, supra*, at p. 817.) Federal Express claims that the jury awarded compensatory damages for bad faith, arguing that such damages are, notwithstanding federal preemption, beyond those permitted by Brandt. PSL contends that the jury awarded no more than attorney fees reasonably incurred in compelling Federal Express to provide the coverage it refused in bad faith.[5]

Brandt damages are not awarded in routine breach-of-contract actions. They are also the result of California common law, which qualifies as an "other provision having the force and effect of law" within the meaning of the preemption statute. (*United Airlines, Inc. v. Mesa Airlines, Inc., supra*, 219 F.3d 605, 607.) *Brandt* damages, or

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[5] The parties have not cited, nor has our own research discovered, any reported decisions where *Brandt* damages have been allowed in any context other than insurance. The point is moot, however, in light of the fact that the judgment must be reversed because of federal preemption.

recovery of attorney fees, is not mentioned in the air bill agreement between PSL and Federal Express. This type of damages is thus not a part of the bargain struck by the parties. It must therefore be regarded as an "enlargement or enhancement based on state law or policies external to the agreement." (*American Airlines, Inc. v. Wolens, supra*, 513 U.S. 219, 233.) Moreover, *Brandt* damages are based on a bad faith refusal of an insurer to provide policy benefits, another creature of state common law. (E.g., *Freeman & Mills, Inc. v. Belcher Oil Co.* (1995) 11 Cal.4th 85, 91 [" '[I]n California, the law implies in every contract a covenant of good faith and fair dealing' "]; *Mitchell v. Exhibition Foods, Inc.* (1986) 184 Cal.App.3d 1033, 1043 [same]; *Spindle v. Travelers Ins. Companies* (1977) 66 Cal.App.3d 951, 959 ["the evolvement of the doctrine of the implied covenant of good faith and fair dealing is an expression of public policy in our state"].) The covenant is also extra contractual; it "is implied as a supplement to the express contractual covenants . . . ." (*Waller v. Truck Ins. Exchange, Inc.* (1995) 11 Cal.4th 1, 36.) Conditions implied by law are conditions imposed by law, state law; they are not negotiated by the contracting parties. Claims based on violation of the covenant are therefore preempted. (E.g., *Howell v. Alaska Airlines, Inc.* (Wash.App. 2000) 994 P.2d 901, 903-905; *Osband v. United Airlines, Inc.* (Colo.App. 1998) 981 P.2d 616, 622 and decisions cited; *A.I.B. Express, Inc. v. FedEx Corp.* (S.D. N.Y. 2004) ___ F.Supp.2d ___, ___ [2004 WL 2526293 p. 8 (Nov. 8, 2004)].)

The same is also true for punitive damages. They were not part of the bargain struck by PSL and Federal Express. A creature of statute (Civ. Code, § 3294), the purpose of punitive damages "is a purely *public* one. The public's goal is to punish wrongdoing and thereby to protect

itself from future misconduct, either by the same defendant or other potential wrongdoers." (*Adams v. Murakami* (1991) 54 Cal.3d 105, 110.) "[S]uch damages are *never* recoverable" in routine breach-of-contract cases. (1 Witkin, Summary of Cal. Law (9th ed. 1987) Contracts, § 820, p. 739, italics added; accord, e.g., *Cates Construction, Inc. v. Talbot Partners* (1999) 21 Cal.4th 28, 61 [" 'In the absence of an independent tort, punitive damages may not be awarded for breach of contract "even where the defendant's conduct in breaching the contract was willful, fraudulent, or malicious." ' "]; *Tomaselli v. Transamerica Ins. Co.* (1994) 25 Cal.App.4th 1269, 1286 ["simple breach of contract, no matter how willful and hence tortious, is not a ground for punitive damages"].) An award of punitive damages would therefore also constitute an " 'enlargement or enhancement [of the bargain] based on state law or policies external to the agreement.' " (*Travel All Over the World, Inc. v. Saudi Arabia* (7th Cir. 1996) 73 F.3d 1423, 1432, fn. 8, quoting *American Airlines, Inc. v. Wolens, supra*, 513 U.S. 219, 233; accord, *Deerskin Trading Post, Inc. v. UPS of America, Inc.* (N.D. Ga. 1997) 972 F.Supp. 665, 673; see also *West v. Northwest Airlines, Inc.* (9th Cir. 1993) 995 F.2d 148, 152 ["Since punitive damages by their very nature seek to punish the entity against whom they are awarded, . . . such damages . . . would be contrary to the goals of deregulation."]; *Cleveland v. Beltman North American Co., Inc.* (2d Cir. 1994) 30 F.3d 373, 379 ["punitive damage awards could have a dramatic impact on a carrier's liability and seriously enlarge a shipper's remedy"].)

Nothing in the Ninth Circuit decision of *Charas v. Trans World Airlines, Inc.* (9th Cir. 1998) 160 F.3d 1259, or our decision in *Aquino v. Asiana Airlines, Inc.* (2002) 105 Cal.App.4th 1272 compels a contrary conclusion. The

former held only that "Congress did not intend to preempt passengers' run-of-the-mill personal injury claims" (*Charas v. Trans World Airlines, Inc., supra*, at p. 1261), whereas this case involves neither passengers nor run-of-the-mill tort claims, but what amounts to tort recovery for a breach of contract, something California allows only in the insurance context or when the breach is accompanied by an intentional tort that is independent of the contract. (*Robinson Helicopter Co., Inc. v. Dana Corp.* (2004) 34 Cal.4th 979, 989-990.) *Aquino* likewise involved a passenger—not cargo—and primarily tort causes of action. A breach of contract claim was involved, but we held it could not be determined by summary judgment because there was an undecided question of federal—not state—law that might prohibit the carrier's action in refusing to board passengers for an intercontinental flight; "the [ADA] preempts states from imposing policies that affect an air carrier's prices, routes, or service. There is no indication in the Act that federal policies are likewise preempted." (*Aquino v. Asiana Airlines, Inc., supra*, at pp. 1285-1286 & fn. 13.)

PSL maintains that the basis of its dispute with Federal Express is not with the actual transportation but with the subsequent conduct in handling PSL's repair reimbursement claim. The argument is tempting. But the law of federal preemption does not allow such a distinction. Preemption cases dealing with mail and highway carriers are illustrative of this principle. The Carmack Amendment to the Interstate Commerce Act (49 U.S.C. § 11707) governs liability for property transported by surface carriers. In language almost identical to that it used in *Wolens* to characterize the scope of the ADA's preemption provision, the United States Supreme Court held that the Carmack Amendment precludes augmentation by state remedies that

" 'in anywise enlarge . . . the responsibility of the carrier' for loss or 'at all affect the ground of recovery, or the measure of recovery.' " (*Charleston & Car. R. R. v. Varnville Co.* (1915) 237 U.S. 597, 603, quoting *Missouri, Kansas & Texas Ry. Co. v. Harris* (1914) 234 U.S. 412, 420, 422.) It too has been construed to prevent law being used to " 'enlarge the responsibility of the carrier' " based on how the carrier handles claims for damage to the shipper's property. (*Charleston & Car. R. R. v. Varnville Co., supra*, at pp. 603-604 [invalidating penalty under state statute for failure to pay claim within 40 days; "a state law is not to be declared a help because it attempts to go farther than Congress has seen fit to go"]; *Gordon v. United Van Lines, Inc.* (7th Cir. 1997) 130 F.3d 282, 289-290 ["the assertion of fraud in the claims handling process is preempted" because "the claims process is directly related to the loss or damage to the goods that were shipped. Indeed, people would not be involved in the process unless either loss or damage had occurred"]; *Rini v. United Van Lines, Inc.* (1st Cir. 1997) 104 F.3d 502, 506 ["Preempted state law claims . . . include all liability . . . stemming from the claims process, and liability related to the payment of claims."]; *Dictor v. David & Simon, Inc.* (2003) 106 Cal.App.4th 238, 247; *Nowakowski v. American Red Ball Transit* (Ill.App. 1997) 680 N.E.2d 441, 443; cf. *Cleveland v. Beltman North American Co., Inc., supra*, 30 F.3d 373 [carrier guilty of "foot-dragging and stonewalling" shippers' claim for damaged property not liable for breach of federal common law duty of good faith and fair dealing; held, Carmack Amendment does not allow federal courts to add common law duties or remedies].) Given that the Carmack Amendment deals with a different aspect of the same subject as the ADA—interstate carriage of goods—and the striking similarity of the construction

made by the Supreme Court, we cannot conclude that a different approach is warranted. There is no logic to granting remedies if shipped by air while denying them if shipped by rail or truck.[6]

However much PSL insists that it is not seeking to recover because of what happened to its equipment while in Federal Express's possession; the contract of carriage cannot be ignored. Without the contract, there would be no declared value coverage, no transportation of PSL's property, no damage, no claim and no delay in paying the claim. It does

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[6] There is recent evidence that Congress intends for air and surface shippers to be treated equally. In 1991 a Circuit Court held that Federal Express—whose operations combined air transport and motor vehicles—qualified as an air shipper for purposes of the ADA. The effect of this decision was that because Federal Express was covered by the ADA's preemption clause, its surface operations were exempted from state regulation. (*Federal Exp. v. California Public Utilities Com'n, supra*, 936 F.2d 1075.) This gave air shippers a competitive advantage over ground-based rivals who remained subject to state regulation. Congress responded with the Federal Aviation Administration Authorization Act of 1994, which, in addition to enacting the current version of the ADA preemption statute, used identical language in a preemption provision for land-based carriers: "Motor carriers of property . . . . [A] State . . . may not enact or enforce a law, regulation, or other provision having the force and effect of law related to a price, route, or service of any motor carrier . . . ." (49 U.S.C. § 14501, subd. (c)(1).) It is exceedingly unlikely in light of this recent history that Congress intends to differentiate between air shippers and surface shippers. If both now share the same exemption, there is no reason to assume that Congress intends for surface shippers' protection under the Carmack Amendment to be greater than the protection given to air shippers by the ADA.

no violence to the English language to conclude that their contract is at the heart of the parties' dispute. Although PSL tries to reframe the issue as far away as possible from the actual movement of its goods, the fact remains that it all goes back to the contract. From this perspective, any judgment against Federal Express is liability for the performance of its services. (E.g., *Read-Rite Corp. v. Burlington Air Express, Ltd., supra*, 186 F.3d 1190, 1196-1197; *Gordon v. United Van Lines, Inc., supra*, 130 F.3d 282, 289-290.) It is also liability imposed and enlarged by California's "own substantive standards" concerning how those services should be performed. (See *American Airlines, Inc. v. Wolens, supra*, 513 U.S. 219, 232-233.) Even if the handling of claims could properly be characterized as "nonessential" to Federal Express's operations, they are "related to" those services, they have "a connection with or reference to" those operations. (See *American Airlines, Inc. v. Wolens, supra*, at p. 228; *Morales v. Trans World Airlines, Inc., supra*, 504 U.S. 374, 384.) They are thus within the preemption of state remedies ordered by Congress.

II

Even if there was no ADA preemption, there would be another insurmountable impediment to affirming the judgment. Preemption or no, the rule of decision to be applied would come from a doctrine of federal common law.

"[F]ederal common law is truly federal law in the sense that, by virtue of the Supremacy Clause, it is binding on state courts" (19 Wright, Miller & Cooper, Federal Practice & Procedure (2d ed. 1996) Federal Common Law, § 4514, p. 453, fn. omitted; *Banco Nacional de Cuba v. Sabbatino* (1964) 376 U.S. 398, 426; *Wayne v. DHL Worldwide Express* (9th Cir. 2002) 294 F.3d 1179, 1184). Long before passage of the ADA, a doctrine of federal

common law known as the "declared value" or "released value" doctrine limited a shipper's recovery for cargo or personal property that was lost, damaged, or destroyed while in the care of a carrier subject to federal regulatory jurisdiction.

A good statement of the doctrine may be found in *Kemper Ins. Companies v. Federal Exp. Corp., supra,* 252 F.3d 509, 512: "Although traditional common law forbade a carrier from disclaiming liability for its own negligence [citation], the released value doctrine allows an air carrier to 'limit [its] liability for injury, loss, or destruction of baggage on a "released valuation" basis.' [Citations.] In exchange for a lower shipping rate, the shipper is deemed to have released the carrier from liability beyond a stated amount. [Citation.] However, the shipper is bound by this agreement only if (i) he has reasonable notice of the rate structure and (ii) he is given a fair opportunity to pay a higher rate in order to obtain greater protection." Once the carrier has complied with these requirements, its liability "cannot exceed the released value regardless of the degree of the carrier's negligence." (*Deiro v. American Airlines, Inc.* (9th 1987) 816 F.2d 1360, 1366.)

Originally formulated by federal courts as general common law under *Swift v. Tyson* (1842) 41 U.S. 1, the doctrine survived *Erie R. Co. v. Tompkins* (1938) 304 U.S. 64, as part of the federal common law. Its application expanding with the scope of federal regulation, the doctrine applies to the states and to suits filed in state courts. (E.g., *New York, N. H. & H. R. Co. v. Nothnagle* (1953) 346 U.S. 128, 131-136; *Adams Express Co. v. Croninger* (1913) 226 U.S. 491, 505-506; *Hart v. Pennsylvania Railroad Co.* (1884) 112 U.S. 331, 337-338; *Read-Rite Corp. v. Burlington Air Express, Ltd., supra,* 186 F.3d 1190, 1195-

1196; Moore, The Law of Carriers (1906) Limitation of Liability, pp. 356, 360; Ray, Negligence of Imposed Duties, Carriers of Freight (1895) § 52, pp. 208-209.)

The ADA left in place a savings clause providing: "Nothing in this chapter shall in any way abridge or alter the remedies now existing at common law or by statute, but the provisions of this chapter are in addition to such remedies." (49 U.S.C. App., former § 1506 (Pub.L. 85-726 (Aug. 23, 1958) 72 Stat. 798), current version at 49 U.S.C. § 40120, subd. (c).) Courts have construed this provision as permitting continued application of the released value doctrine to non-routine breach of contract actions subsequent to the ADA and *Wolens*. (E.g., *Read-Rite Corp. v. Burlington Air Express, Ltd., supra*, 186 F.3d 1190, 1195-1197; *Sam L. Majors Jewelers v. ABX, Inc.* (5th Cir. 1997) 117 F.3d 922, 928-931; *First Pennsylvania Bank v. Eastern Airlines, Inc.* (3d Cir. 1984) 731 F.2d 1113, 1122; *King Jewelry, Inc. v. Federal Exp. Corp., supra*, 166 F.Supp.2d 1280, 1283; *Welliver v. Federal Exp. Corp.* (S.D. N.Y. 1990) 737 F.Supp. 205, 207.)[7]

PSL submits that it should not be bound by the declared value figure it and Federal Express fixed in the airbill. It reasons that "Were a carrier permitted to sell such

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[7] California courts applied the release value doctrine prior to passage of the ADA (*Donlon Bros. v. Southern Pacific Co.* (1907) 151 Cal. 763, 770-775; *Michalitschke v. Wells, Fargo & Co.* (1897) 118 Cal. 683, 688-689; *Muelder v. Western Greyhound Lines* (1970) 8 Cal.App.3d 319, 324-325; see Civ. Code, § § 2176, 2178) and after (*Dictor v. David & Simon, Inc., supra*, 106 Cal.App.4th 238, 245-249; *HIH Marine Ins. Services, Inc. v. Gateway Freight Services, supra*, 96 Cal.App.4th 486, 492-494).

[additional] coverage yet avoid the obligation to adjust claims in good faith and still limit its liability, the declared value doctrine would become a dead letter. . . . Stated otherwise, if FedEx were free to commit a bad faith breach of its obligations under its declared value coverage contract, it would effectively deny its customers a fair opportunity to obtain the benefits of coverage they thought they were purchasing." But that coverage, although long-delayed and grudgingly delivered, was not illusory. Because PSL did purchase additional "declared value" protection from Federal Express, and did ultimately receive its benefits, the liability limitation for the amount declared satisfies the released value doctrine. It is consequently valid and enforceable. (See *Read-Rite Corp. v. Burlington Air Express, Ltd., supra*, 186 F.3d 1190, 1198-1199.)

Confronting a situation almost identical to that endured by PSL, one federal appellate court stated: "Ordinarily, common law principles of equity leaven the law, softening its rigors so that the law's aim of administering justice fairly is not lost. But on occasion, and this is one, the equities urge a course that the law may not take." (*Cleveland v. Beltman North American Co., Inc., supra*, 30 F.3d 373, 374.) We find ourselves similarly hamstrung. Although the supremacy of federal law requires that Federal Express prevail, we cannot refrain from expressing our dismay at this result. However, the statutory command that states stay out of this field, as twice expansively construed by the United States Supreme Court, is unambiguous. So is the released value doctrine of federal common law that would in any event have to be applied and which would also absolve Federal Express from paying any more than the contractual amount it has already turned over to PSL.

The judgment is reversed. The parties shall bear their respective costs of appeal.

_____

Kay, P.J.

We concur:

_____

Sepulveda, J.

_____

Rivera, J.

Trial Court: Alameda County Superior Court

Trial Judge: Honorable Patrick J. Zika

Counsel for Defendant and Appellant:

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App. 20

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FILED
APR 22 2005
Court of Appeal - First App. Dist.
DIANA HERBERT
By _____
Deputy

POWER STANDARDS LAB, INC.,
Plaintiff and Respondent,
v.
FEDERAL EXPRESS CORPORATION,
Defendant and Appellant.

A103021
Alameda County No. C841938

BY THE COURT:

The petition for rehearing is denied.

Date: APR 22 2005 KAY, P.J. P.J.

App. 21

Court of Appeal, First Appellate District, Division Four – No. A103021

S133597

IN THE SUPREME COURT OF CALIFORNIA

En Banc

POWER STANDARDS LAB INCORPORATED, Plaintiff and Respondent

v.

FEDERAL EXPRESS CORPORATION, Defendant and Cross-complainant.

Petition for review DENIED.

SUPREME COURT
F I L E D
JUL 27 2005

Frederick K. Ohlrich Clerk

Deputy

/s/

Chief Justice